

Draft Report



South Somerset District Council

► Section 106 & Commuted Sums

Issued to: Donna Parham
Head of Financial Services

Simon Gale
Head of Planning

Ian Clarke
Head of Legal

Gerry Cox
Head of Audit Services

Working in partnership with



Date of Report: December 2008

Issued by: Scott Freeborn
Principal Auditor

Section 106 & Commuted Sums

Introduction and Scope

This audit review was undertaken at the invitation of management in response to a perceived need to review the manner and methodology of calculating and managing payments to the authority in respect of Section 106 (S106) Agreements concluded as part of the Development Control planning approval process to affirm that the processes and procedures in operation within South Somerset DC are operating in a sound, robust and controlled manner.

In terms of the detailed work undertaken the audit sought to confirm that the Authority has sufficient and adequate policies and procedures in place within the service department and finance to ensure that S106 Agreements are properly and effectively managed to minimise the risk of:

- Financial loss to the Authority
- Legal and Reputational damage to the Authority
- Ineffective use of manpower/resources

S106 Agreements are a key aspect of most major planning development approvals granted by the Authority. The items captured within S106 Agreements deal with the additional infrastructure costs that will be incurred within the area of the Authority arising from the completion of a development. Depending on the scale of the proposed development the sums of money associated with a S106 Agreement can be considerable.

This may take the form of changes to highways, contributions toward increased schools provision, creation/maintenance of open spaces, recreational areas and so on. The costs arising from these are often significant and require negotiation and settlement between the planner and the developer, through use of nationally agreed formulae.

How these are delivered also varies, depending on the requirement i.e. the developer may be charged with completing the work directly, County will undertake highways works and educational provision, and the District open spaces, recreational provision etc.

By their very nature S106 Agreements require specified actions to take place within a pre-defined timescale, most often as works undertaken by an Authority in return for payment received from developers, the start date of which is in turn determined by the point at which development commences.

In principle the overall financial impact to the Authority will be cost neutral in budgetary terms (i.e. an action required to be performed will be entirely funded through S106 contributions) with finance received from developers ring-fenced for completion of the agreed actions. In practice S106 Agreement monies may be augmented by contributions from the Local Authority to incorporate additional activities to address infrastructure issues for pre-existing development.

Management Summary

The settlement of S106 Agreements forms an important element of the planning process, particularly for substantial developments that impact in a significant manner on the infrastructure of the district in terms of services/amenities that have to be provided road structures etc. Often the actions required are significant and the sums of money required to accomplish them substantial. Audit testing indicates that the process of determination and agreement of the S106 conditions are performed within prescribed national guidelines and formulae.

As a result of completing this audit the overall opinion formed was that individual aspects of the securing of S106 agreements are pursued diligently by the Council.

However, once an agreement has been concluded there are inadequate and ineffectual mechanisms in place to ensure that the agreed conditions are applied or enforced as necessary.

As the amounts of money involved are significant this is of key importance to the Authority.

A key factor that has to be remembered is that S106 Agreements form part of the process of granting planning permission. The terms of the S106 Agreement typically however do not come into force until such time that the approved development actually takes place. Most planning approvals allow a period of up to five years before lapsing and development may be initiated at any time within this. Therefore a S106 agreement may lie latent for some considerable time before 'activating'. This complicates the process of monitoring and compliance.

The key risk elements identified are:

1. Maintenance Payments and Commuted sums - At present there are no procedures in place nor are there any officers responsible for the monitoring or collection of Commuted sums
2. Monitoring and collection of monies as they fall due and completion of obligations by authority - There are no mechanisms or procedures in place for the monitoring or pursuit of payments where they have not been made or agreed actions by the council in exchange for S106 payments.
3. Budgetary Control – S106 funds aggregated within accounting structure, rendering it difficult to see how and if monies applied.
4. Enforcement of Conditions - S106 monies received and inappropriately applied or works undertaken by Authority but funds not received – Ineffectual mechanisms for ensuring compliance with s106 conditions, no reconciliation between receipt and application of funds.
5. Management/Monitoring Reports - There are no management reports produced describing the status of S106 agreements.

At the conclusion of the review I am able to affirm to management that the professional activities of officers in calculating, negotiating, concluding and recording income received for S106 agreements is undertaken in a diligent, competent and professional manner. However, the Council is at risk, through the lack of a general co-ordinating and monitoring mechanism, of failing to manage and enforce the terms of negotiated S106 agreements. Although S106 should always be cost-neutral to the Authority, failure to ensure compliance could result in SSDC having to subsequently finance the cost of undertaking infrastructure activities that should have been funded by the developer.

The principal risk to South Somerset is that should agreed S106 actions not be completed as a result of the Authority failing to ensure they are performed, either the works have to be undertaken and funded entirely from SSDC finances, or finance provided by developers has to

be handed back (with interest) because SSDC has failed to complete the works within the agreed period.

Recommended Actions

In response to the issues found arising from the audit I have identified a number of areas where actions can be undertaken to strengthen controls enabling South Somerset to attain a reasonable measure of assurance that the Authority has fully discharged its responsibilities in respect of S106 Agreements entered into as part of the Development Planning Approval process.

Normally a series of discrete recommendations would be made to address each individual issue identified. In this case however, it is more appropriate to make a number of more general conclusions/recommendations to management as the issues identified are typically cross-cutting corporate matters rather than individual tasks that can be given to ascribed to individual service managers. It is my opinion that a working group made up of representatives from Legal, Finance, Planning and other key stakeholder services to develop the following:

1. There needs to be some form of corporate database or similar record process put in place. This would serve the following purposes:
 - Ensure all S106 Agreements (and actions arising) are identified – Legal services to populate the data from records of current S106 Agreements and append new Agreements as and when entered into
 - Identify dates and timescales when actions by either the developer or the Authority have to be commenced and completed – this would also serve as a potential trigger for establishing whether enforcement action is required.
 - Allow use of planning application case number as unique reference number across SSDC
 - All service departments/areas with actions/responsibilities arising from S106 Agreements become aware of the need to undertake and complete them within the agreed time
 - Facilitate the development and implementation of a system of management monitoring reporting to facilitate high-level and more detailed tracking of S106 obligations and the funds associated with them. Suggested quarterly reporting to Management Board and monthly, as required, to specific service managers
 - Track funding due from developers is received when due and expenditure correctly allocated to meeting agreed S106 actions.
2. To ensure that any database, or such recording/monitoring system, implemented will be properly embedded into the ongoing operational practices of the Authority there will be a need to raise awareness to and training on its use, with assignment of responsibilities and ongoing maintenance.
3. Current accounting practice of recording all S106 income against a single ledger code to be improved by the creation of detailed subjective codes (one per agreement identified by unique planning case reference number) to enable precise tracking of income received and expenditure incurred.
4. In respect of commuted sums, Finance department to review the current 'equal annual portions' methodology for allocating budget to service departments to undertake agreed maintenance to better address the effects of annual inflation and the increasing negative impact this has on service budgets.
5. Finance to review the existing S106 funds and populate the developed database with details to enable management to take stock on the current status of the related agreements.

Summary of Key Findings

1. Maintenance Payments or Commuted Sums

Maintenance Payments or Commuted Sums as they are referred to are a statutory requirement as per Town and Country Planning Act and Highways Act 1980 that requires developers to cover some of the future maintenance costs of certain areas or items that are going to be adopted and maintained at public expense; it is the responsibility of the Planning Authority to claim these payments.

At present there are no procedures in place nor are there any officers responsible for the monitoring or collection of Commuted sums. There are various spreadsheets used in various different parts of the Council but there is no centralised database of these funds.

An example obtained from a finance officer was that a commuted sum was paid to the Authority by a developer to meet future years maintenance costs and the service had applied for the annual sum to be added to the section's revenue budget even though the facility that the sum applied to had not yet been constructed, it was only once the finance officer discovered and pointed out the omission that the funds were not added to the revenue budget.

There is a risk that the Council is losing sums of revenue that it is entitled to or the sum is being applied to the service department before the purpose the commuted sum was obtained for has been realised.

From discussion with a Senior Officer it was found that there is no process in place for the monitoring of payments made against Commuted sums. All money received is used as a central 'pot' of money against which maintenance is charged.

What is obvious through discussion with the services is that there is no process in place for the monitoring of payments as services are not aware which funds they should be expecting due to a lack of inter-service communication.

Where the Council as part of the negotiated S106 Agreement includes sums to be paid to other Authorities or statutory agencies I was able to affirm it does not act as an intermediary for the collection and onward transmission of funds, merely as a conduit for the negotiation of funds. Once the S106 has been agreed it is left, for example, to the Education and Highways Directorates at the County Council to pursue the funds they have agreed.

I established via the Principal Accountant and Management Accountant that there is a process in place for the monitoring of Commuted sums actually received with all being entered on to a spreadsheet which is monitored by the Management Accountant. The money received is divided by the number of years specified within the S106 agreement and is then paid to the service as a revenue budget on an annual basis.

It was noted that this apportionment takes no account of the effects of inflation, so, to use a hypothetical example, if a commuted sum of £20,000 is received to cover say grounds maintenance costs for 20 years all accountancy would do is divide one into the other and then make a budget provision of £1,000 a year. No account is taken of inflation, what costs £1,000 in year one will not cost the same in year twenty – a simple calculation indicates that at a notional 3% annual inflation rate to achieve the same purchasing power £1,755 is required by year twenty. Therefore year on year this differential will grow with the difference being met from SSDC's service revenue budget. However, equally no account is made of the interest accrued on the reducing balance of the commuted sum over time. When calculated out based

upon the premise that SSDC can invest money at a minimum of equal to the rate of inflation it is found that the annual payments can be increased for inflation yet remain cost neutral to the Authority as demonstrated in the following chart.

Committed sum annual payment calculation

Principal received 20000 Investment rate 3.00%
 Period of Agreement 20 inflation rate 3.00%

Existing method (reducing balance)

Year	Payment	Balance
1	1000	19000
2	1000	18000
3	1000	17000
4	1000	16000
5	1000	15000
6	1000	14000
7	1000	13000
8	1000	12000
9	1000	11000
10	1000	10000
11	1000	9000
12	1000	8000
13	1000	7000
14	1000	6000
15	1000	5000
16	1000	4000
17	1000	3000
18	1000	2000
19	1000	1000
20	1000	0
	<u>20000</u>	

Inflation/Interest Adjusted model

Year	Payment	Balance	Interest Accrued on Fund	New Balance
1	1000	19000	570	19570
2	1030	18540	556	19096
3	1061	18035	541	18576
4	1093	17484	525	18008
5	1126	16883	506	17389
6	1159	16230	487	16717
7	1194	15523	466	15988
8	1230	14758	443	15201
9	1267	13934	418	14353
10	1305	13048	391	13439
11	1344	12095	363	12458
12	1384	11074	332	11406
13	1426	9980	299	10280
14	1469	8811	264	9076
15	1513	7563	227	7790
16	1558	6232	187	6419
17	1605	4814	144	4959
18	1653	3306	99	3405
19	1702	1702	51	1754
20	1754	0	0	0
	<u>26870</u>			

With the current methodology of allocating commuted sum payments to service departments there is a risk that insufficient budget is provided over time to cover the true cost of agreed actions as per the S106 Agreement, and the shortfall from which then has to be made good from elsewhere within the service departments budget to the potential detriment of other service provision.

2. Monitoring and collection of monies as they fall due and completion of obligations by Authority

I can confirm that there is no central database of key dates and that once an agreement has been signed there does not appear to be any co-ordinated approach to the monitoring and collection of monies agreed under the terms of S106 Agreements.

Through discussion with officers in various service areas it was affirmed that there are no mechanisms or procedures in place for the monitoring or pursuit of payments where they have not been made. It has been acknowledged that there are inadequate controls in place for the monitoring of S106 agreements after they have been agreed and signed.

Legal Services maintain a spreadsheet which records all of the completed S106 agreements, but this does not contain a list of trigger dates nor detail what was agreed within the S106 agreement. This spreadsheet, recording all Agreements completed in recent years, would

form the useful data source from which a corporate management/monitoring system could be developed.

Legal services do attempt to advise service managers of their S106 Agreement obligations, particularly where there have been personnel changes during the life of the agreement, but this is essentially for those where other issues have given the development a raised profile within the Authority.

The process of services claiming/applying funds is hampered by a lack of inter-service communication. There is no effective system in place to monitor whether funds have been received, are being spent appropriately or will be completed within the specified timescale within the Agreement with the risk that the developer will require monies refunded, with interest.

There is a financial risk the Council due to a lack of adequate monitoring of trigger points and the pursuit of staggered payments. Legal services have indicated that a Somerset wide review of S106 Agreements is currently in progress included in which is the proposal that the wording of future Agreements be amended so that the onus is placed upon the Developer to notify/act/make payment at the appropriate time, and where this is not done, any additional costs incurred by an Authority can additionally be recovered from the Developer.

3. Budgetary Control

Through discussion with the Management Accountant and the Principal Accountant it was established that services do not have specific S106 budgets, although there is a central budget which can be spent against.

In its current iteration there is a ledger account code against which all income received and payments made are recorded. In essence the fund is used as a large pot of money with codes created once a project has been initiated. However this method of accounting for S106 Agreement funds complicates the issue of monitoring under/over spends of funds and also makes it difficult for services to account for the money they have available - if any, for the projects they have agreed to undertake.

There is a financial and legal risk to the Council if money is spent against a project before/without the money first being paid to the Council and a developer subsequently challenges the Authority regarding the use of money provided under S106 Agreements

This can readily be addressed by the development of appropriate (project) detail codes against which income received and expenditure incurred can be recorded. This information will enable management to monitor the flow of funds across the life of the Agreement and highlight at an early point any deviation from the budget profile.

4. Enforcement of Conditions - S106 monies received and inappropriately applied or works undertaken by Authority but funds not received.

I affirmed that the Planning team in conjunction with the Legal team are responsible for managing the completion of the S106 agreements. The role of the planning team is one of negotiator and specialist who will advise the relevant services of their rights and the limits of their claims/request for funds to meet obligations arising from the development if approved.

Legal services are responsible for finalising the agreement on behalf of the Council with the developer based upon the terms agreed by planning. Once all issues between the Council and the developer have been resolved Legal will then prepare a formal agreement from the details supplied. This may take several iterations with the developer's legal representative

where there is an issue over the form of the agreement requiring Legal to refer it back to Planning and/or the service concerned for resolution. Once the agreement has been completed Legal will get copies of the document signed by the Council and the developer. There is communication between legal/planning/stake holders to confirm the signing/implementation of S106 Agreements.

From my discussions with the officers involved in the various stages of the process I am able to confirm that the process of negotiating and settling a S106 Agreement is rigorously applied.

However, it is in the period after this stage is reached where the Council's coordinated approach loses some of its integrity. From enquiries made I found that there is no corporate coordinated approach to ensure that the terms of the S106 Agreement made as part of the planning approval are completely complied with.

The risks are:

- Developer fails to adhere to S106 Agreement
 - There is a risk that the obligations placed upon the Developer in the S106 Agreement will not be adhered to. For example, money due to be paid for provision of community facilities, in whole or part of a bigger scheme, will not be paid over, potentially the community loses out through lack of provision of these facilities or the Council suffers financial loss as they pay for the facilities without recovering the S106 funds that should have been used to cover the costs. Similarly, there may be non-financial requirements that are not complied with, e.g. play areas not constructed by developer or affordable housing units sold on the open market.
 - Establishing whether a S106 planning condition has been met is extremely difficult due to a lack of recorded trigger points within the Council, and also due to the difficulty of knowing that trigger points have been reached - for example have 50 new dwellings in a development become inhabited thus triggering/kicking off the requirement for construction of play facilities?
 - It was also established through discussion with officers from both planning and leisure services that there are currently issues with regard to the monitoring and enforcement of S106 Agreements that have been ignored. Until such time that this area is strengthened prevention of future occurrences will be down to the memory and skill of individual officers rather than a control being in place to prevent such a situation.
- The Council fails to monitor completion of agreed actions paid for by S106 funds
 - There is no effective method of monitoring the use of S106 funds received by the Council. Audit has become aware of at least one scheme where developer funds have been received and implementation of the agreed actions by the service section concerned is lagging so far behind overall expectations there is concern over the ability of the Council to complete within the timescale defined by the Agreement.

The issue is whether Legal or Planning Enforcement or some other service is responsible for monitoring, and enforcement, of planning development (S106) conditions. Or, more appropriately, as S106 Agreements often cut across several service areas that the management of S106 Agreements be process mapped and rather than identify an individual officer as responsible for overseeing and monitoring, procedural mechanisms and reporting

points be embedded in the system where individual service officers are identified and required to assume responsibility for those aspects that are within their direct domain.

There is a risk that the community does not receive facilities it is entitled as they were not provided due to a lack of enforcement and monitoring of S106 Agreements by the Council.

There is a residual financial as well as legal risk to the Council where a developer who has paid the agreed sum to the Council asks for its return, with interest, when the period of the Agreement is concluded and actions by the Council in return for the payment have not occurred. Audit has become aware of correspondence received by the Council from legal firms representing developers seeking to affirm that actions to be undertaken by the Council in exchange for S106 payments have been completed as stipulated. There was speculation that these firms have spotted a market niche where in exchange for a percentage fee recovery on behalf of the developer will be sought for S106 actions paid for but not completed.

5. Management/Monitoring Reports

Through discussion with the Head of Planning and other service heads I confirmed that there are no management reports produced describing the status of extant S106 agreements.

In my opinion there should be regular management reports produced dealing with all S106's signed and brought into effect with the granting of planning approval. Reports produced should capture on a development by development basis, agreed actions (by both the Developer and Authority); trigger points, deadlines and conditions agreed within the agreements(together with status indicators on actions to be completed by SSDC); and the outstanding conditions that are yet to have been triggered/complied with.

The Authority is exposed to the risk that management are unaware of the progress of S106 agreements both in terms of the Developer's obligations and the Authority's (i.e. funds received to perform specified works) and will subsequently be unable/unaware whether additional resources and/or expertise are required to ensure compliance. Non compliance may require the Authority to return to Developers significant sums of money.

Acknowledgements

I would like to express my gratitude for the assistance and co-operation of the Heads of Finance, Legal and Planning together with several service managers during the conduct of this audit.

Scott Freeborn
Principal Auditor

December 2008